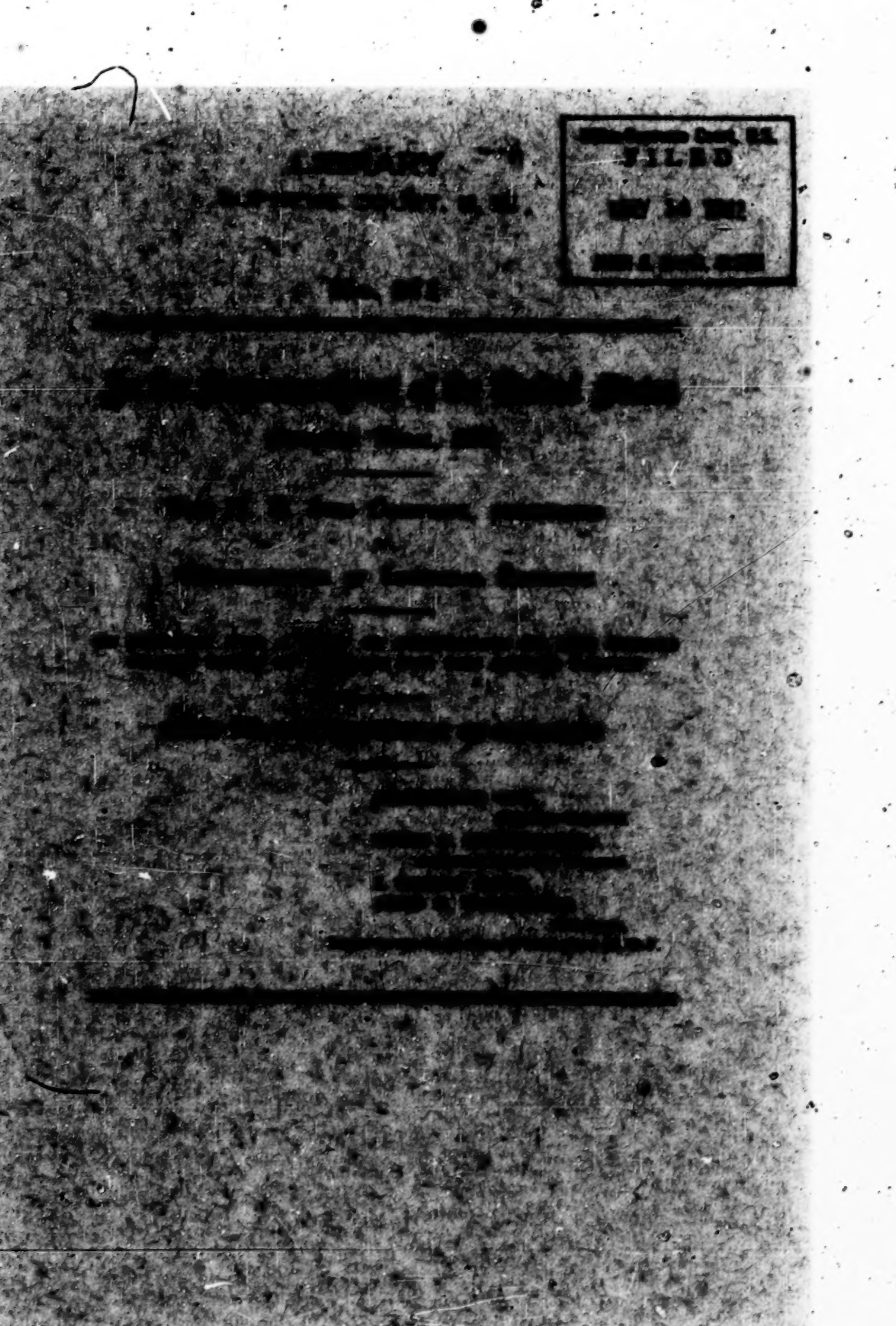

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In the Supreme Court of the United States

OCTOBER TERM, 1961

No. 871

THE H. B. IVES COMPANY, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The memorandum findings of fact and opinion of the Tax Court (Pet. 11–15) are not reported.[1] The opinion of the court of appeals (Pet. 17–20) is reported at 297 F. 2d 229.

JURISDICTION

The judgment of the court of appeals (Pet. 20–21) was entered December 28, 1961. A petition for rehearing (Pet. 21–23) was denied on January 16, 1962 (Pet. 24). The petition for a writ of certiorari

[1] The petition cites 30 T.C. 295 as the report of the Tax Court opinion; actually this is the citation to the Tax Court opinion in *Champion Spark Plug Co.* v. *Commissioner* (discussed *infra*, p. 7).

was filed April 13, 1962. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

QUESTION PRESENTED

Whether, as the court below held, taxpayer's obligation for the purchase of annuity contracts for four employees did not accrue until 1954, when taxpayer executed the contracts with the insurance company—there being no underlying legal obligation to the employees—or, whether, on the contrary, as the Tax Court held, this obligation accrued in 1953, when taxpayer's directors adopted a resolution that a sum be set aside immediately for purchase of the annuities and that its president negotiate with various insurance companies to enter into the annuity contracts.

STATUTE INVOLVED

Internal Revenue Code of 1939 (26 U.S.C. 1952 ed.):

SEC. 23. DEDUCTIONS FROM GROSS INCOME.

In computing net income there shall be allowed as deductions:

(a) [As amended by Sec. 121(a) of the Revenue Act of 1942, c. 619, 56 Stat. 798] *Expenses.*—

(1) *Trade or business expenses.*—

(A) *In General.*—All the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business, including a reasonable allowance for salaries or other compensation for personal services actually rendered; * * *

* * * * *

SEC. 43. PERIOD FOR WHICH DEDUCTIONS AND CREDITS TAKEN.

The deductions and credits (other than the corporation dividends paid credit provided in section 27) provided for in this chapter shall be taken for the taxable year in which "paid or accrued" or "paid or incurred", dependent upon the method of accounting upon the basis of which the net income is computed, unless in order to clearly reflect the income the deductions or credits should be taken as of a different period. * * *

STATEMENT

In 1951 petitioner, The H. B. Ives Company, created a group life annuity plan for the purpose of providing retirement benefits for its employees who were under the age of 70 years. At a directors' meeting on November 24, 1953, the petitioner's president advised the board that four long-service employees were excluded from the plan merely because they happened to be over 70 at its inception. He stated further that "he felt we were really obligated to give these (ineligible) employees equivalent benefits, and he had contacted an insurance agent who had recommended the immediate purchase of annuities to take care of the company's obligation" (Pet. 12–13). The directors thereupon adopted the following resolution (*ibid.*):

> Resolved that the sum of $22,000.00 be appropriated and set aside immediately for the purchase of annuity contracts for the four (ineligible) employees, that the President be au-

> thorized to negotiate with various insurance companies and enter into the necessary annuity contracts to accomplish the purpose of the resolution, and that the moneys hereby appropriated and set up as a liability of the corporation as of this date and that negotiation with the insurance company be completed prior to February 15, 1954 when the first additional (ineligible) employee will retire.

Thereafter, petitioner's president negotiated with an insurance company which issued the annuity contracts on January 15, 1954 (Pet. 4). On the same date the insurance company sent petitioner an invoice for the contracts in the amount of $22,100.42, which was paid by petitioner on February 16, 1954 (Pet. 13–14).

Petitioner, which kept its books and made its income tax returns on an accrual method of accounting and on a calendar year basis (Pet. 12), made the following entry on its books as of December 31, 1953 (Pet. 14):

Dr. Pensions Paid	$22,463.89	
Cr. Accounts Payable		$22,463.89

It also deducted $22,463.89 as a business expense on its 1953 return.[2]

The Commissioner disallowed the deduction, determining that it should have been taken in 1954, and petitioner brought this action in the Tax Court to redetermine the deficiency which was assessed. The Tax Court held that the facts of the case could not be

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[2] It was admitted before the Tax Court that $363.47, the difference between the $22,463.89 deducted and the $22,100.42 actually paid, was an erroneous entry. (Pet. 14.)

distinguished from *Champion Spark Plug Co. v. Commissioner*, 30 T.C. 295, affirmed, 266 F. 2d 347 (C.A. 6), and that accordingly the accrual of the liability was properly deductible in 1953, "the time the obligation was incurred as it was in the Champion case" (Pet. 15).

The court of appeals reversed, holding that petitioner was under no obligation to pay the insurance company until the contracts were executed in 1954, and that before that time petitioner was subject to no underlying legal obligation to the four employees. Since the obligation to pay was not certain until 1954, the court below held the expenditure was not "paid or incurred" in 1953 within the meaning of Section 23(a)(1)(A) of the 1939 Code (Pet. 19–20).[*]

ARGUMENT

The decision below is correct; it is not in conflict with *Commissioner v. Champion Spark Plug Co.*, *supra*, or any decision of this Court or the courts of

[*] The Commissioner had contended alternatively that even if the obligation to purchase the annuities was found to have become fixed in 1953 so as to permit its accrual in that year, Section 23(p)(1)(D) of the 1939 Code precluded the deduction until the year of actual payment, 1954. That Section provides that compensation paid or accrued on account of any employee under a plan deferring the receipt of such compensation is deductible "in the taxable year when paid." The Tax Court rejected this contention on finding that "petitioner's purchase of the annuity contracts * * * did not represent compensation for past services and was not a method which had the effect of an annuity plan or similar plan deferring the receipt of compensation" (Pet. 14). Respondent made the same contention in the court of appeals which did not rule upon the point in view of its holding that the petitioner's obligation to purchase the annuities did not become fixed until 1954.

appeals, and no question is presented warranting review.

1. The deduction for ordinary and necessary business expenses allowed by Section 23(a)(1)(A) of the Internal Revenue Code of 1939 (*supra*, p. 2) is for such expenses "paid or incurred" during the taxable year. Section 43 (*supra*, p. 3) adds that deductions shall be taken for the taxable year in which paid or accrued or paid or incurred "dependent upon the method of accounting upon the basis of which the net income is computed." Under principles well established by decisions of this Court, in the case of an accrual basis taxpayer, a liability is to be reported no earlier than the year when all events occur which determine the liability to pay and fix the amount of the liability. A taxpayer may not accrue an expense, the liability for which is contingent. *United States* v. *Anderson*, 269 U.S. 422; *American National Co.* v. *United States*, 274 U.S. 99; *Niles Bement Pond Co.* v. *United States*, 281 U.S. 357; *Aluminum Castings Co.* v. *Routzahn*, 282 U.S. 92; *Dixie Pine Co.* v. *Commissioner*, 320 U.S. 516, 519; *Security Mills Co.* v. *Commissioner*, 321 U.S. 281, 284; *United States* v. *Olympic Radio & Television*, 349 U.S. 232; United *States* v. *Consolidated Edison Co.*, 366 U.S. 380, 385.

Applying these principles, the liability to make the payment for the annuity contracts did not become certain until 1954, when the contracts were executed. There was no pre-existing legal liability to the four employees and the resolution of November 24, 1953,

merely "appropriated and set aside" the sum of $22,000 "for the purchase of annuity contracts" for the four ineligible employees, and "authorized" the president "to negotiate with various insurance companies and enter into the necessary annuity contracts to accomplish the purpose of the resolution" (Pet. 13); it created no obligation. Nor did the entry by petitioner upon its books impose any obligation upon it; such an entry was plainly revocable at its will.

2. There is no merit to petitioner's assertion that the decision of the Second Circuit below conflicts with *Commissioner* v. *Champion Spark Plug Co.*, 266 F. 2d 347 (C.A. 6). There, the Sixth Circuit, affirming the Tax Court, held that the resolution imposed a definite and unconditional obligation on the corporation to pay a fixed amount in installments (commencing the following year) to a totally disabled employee. Based upon that holding, the court allowed the deduction of the entire obligation in the year the resolution was adopted. Here, the court of appeals determined that under the law of a different state a different corporate resolution did not impose a fixed obligation to the four employees concerned and accordingly denied the deduction.

The decisions are entirely consistent insofar as the application of Section 23(a)(1)(A) of the 1939 Code is concerned. And even a direct conflict—not present here—on the question whether the particular resolutions imposed fixed and definite obligations to the employees, would not warrant review by this Court.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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MAY 1962.